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In the Supreme Court
OF THE
United States

OCTOBER TERM, 1932

Nos. 129, 130, & 131

JOHN FREULER, Administrator of the Estate of Louise P. V. Whitcomb, Deceased,
Petitioner,
vs.
DAVID BURNET, Commissioner of Internal Revenue,
Respondent.

(CCA 68

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(CCA 6

PETITION FOR WRITS OF CERTIORARI to the United States Circuit Court of Appeals for the Ninth Circuit and BRIEF IN SUPPORT THEREOF.

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PETITION FOR WRITS OF CERTIORARI
to the United States Circuit Court of Appeals for the Ninth Circuit.

To the Honorable Charles Evans Hughes, Chief Justice of the United States, and to the Associate Justices of the Supreme Court of the United States:

The undersigned, on behalf of the above-named petitioner, pray that writs of certiorari issue to review the judgments of the Circuit Court of Appeals for the Ninth Circuit entered on January 9, 1933, in the three cases between the above named parties, docketed therein as Nos. 6833, 6834 and 6835.

OPINIONS BELOW.

The opinion of the Board of Tax Appeals (R. 32) is reported in 22 B. T. A. 118. The opinion of the Circuit Court of Appeals (R. 154-160) is reported in 62 F. (2d) 733.

JURISDICTION.

The judgments of the Circuit Court of Appeals were entered January 9, 1933. By order of Mr. Justice Sutherland, dated March 16, 1933, the time for filing of these petitions has been extended to June 8, 1933.

The jurisdiction of this court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED.

These cases involve the question whether certain amounts which the petitioner and his decedent received in the years 1921-1925, inclusive, were income taxable to

them in those years under Section 219 of the Revenue Act of 1921, and Section 219 of the Act of 1924. The amounts in question were actually paid by the trustee of a testamentary trust to the taxpayers, beneficiaries of the trust, as income. Thereafter the state court having jurisdiction over the accounts of the trustee held that the amounts in question should not have been paid to the taxpayers but should have been retained by the trustee as a reserve for depreciation of certain property which produced the revenue. The state court decreed that the petitioner repay the amounts in question.

There are two questions presented, one involving the construction of the statutes and the other involving the effect to be given by the federal courts to the decree of the state court.

STATUTES INVOLVED.

The statutes involved are Section 219 of the Revenue Act of 1921 and Section 219 of the Revenue Act of 1924. All pertinent provisions of these sections are printed in the appendix, pages i to viii, *infra*. The most important provision of the 1921 Act is that

> "there shall be included in computing the net income of each beneficiary that part of the income of the estate or trust for its taxable year which, pursuant to the instrument or order governing the distribution, *is distributable to such beneficiary, whether distributed or not.*"

STATEMENT.

The above petitions involve income taxes asserted against the administrator of the estate of Mrs. Whitcomb for that part of the year 1921 in which she was alive and also for the rest of 1921, for 1922, 1923, 1924 and 1925. There is, however, no substantial difference in the facts as to the different years. After her death, her estate received part of the income from the trust. The following epitome of the facts in the case in which the court below handed down the opinion (involving the part of the taxable year 1921 when Mrs. Whitcomb was alive) indicates substantially the situation in each of the cases. The facts therein set forth appear in the unchallenged findings of the Board of Tax Appeals or in uncontradicted evidence.

A. C. Whitcomb died domiciled in California in 1889 (R. 34). By his will, which was duly probated there, he left the residue of his estate in trust to pay his widow, the decedent, one-third of the interest or income for life, and to pay the rest of the income to other persons, with remainder over (R. 34-35). The residue consisted largely of cash, bonds, stocks and notes and of some improved real estate (R. 35). In 1906 the San Francisco fire destroyed the improvements on certain of the real estate (R. 35-36). The trustee then adopted a policy of building very substantial improvements, acquiring additional real estate and selling other assets of the trust to raise cash for this end (R. 36). He erected minor improvements in 1906, major improvements from 1910 to 1913, including the Whitcomb Hotel, and later other improvements (R. 70-72). A substantial part of the principal of the trust estate was invested in furniture for the hotel (R. 36).

The Whitcomb Hotel and its furniture and equipment alone represented an investment of more than two million dollars (R. 36). During each of the taxable years here involved, the improvements and furniture suffered substantial exhaustion, wear and tear (R. 36). The exact amount of the depreciation for each year was specifically found by the Board. During 1921 alone the depreciation was in excess of $43,000 (R. 36).

The trustee, however, did not withhold from the beneficiaries to whom payments of income were being made anything on account of this depreciation (R. 37-38). The will contained no express directions in regard to the manner in which the income from the trust should be computed, accounts kept, or depreciation provided for (R. 35).

The trustee, in his fiduciary return for the year 1921 (as well as other years), in computing the net income of the trust, deducted the amount of depreciation sustained by the trust estate; and neither the petitioner nor any other beneficiary included in his or her return of income for 1921 (or the other years), the amount paid by the trustee representing his or her share of the amount deducted on the fiduciary return for depreciation (R. 37, 42).

Later the trustee filed his account with the California state court having jurisdiction over the trust estate and his accounts (R. 38). Remaindermen objected because of the absence of a depreciation reserve (R. 38-39). After a hearing, in which all parties were represented by counsel, the court sustained the objection (R. 39-40) and ordered restoration of such a reserve (R. 41). Petitioner repaid $10,700 (R. 42), which is more than decedent's share of the depreciation for the fractional year 1921 in

question (*supra*, p. 5) (R. 36-37). The excess was due to the fact that the amount of the repayment covered more than this period.

The state court also decreed that thereafter until termination of the trust the trustee should withhold annually as a reserve for depreciation, a reasonable and proper amount from the income of the trust property (R. 41).

The Commissioner of Internal Revenue increased the income shown on the taxpayer's returns by his respective proportionate share of the amount allocated to depreciation, and on that basis asserted deficiencies in his tax (R. 42). The Board of Tax Appeals held that the petitioner was correct in contending that he was not taxable upon the amounts representing depreciation which he and his decedent received and which he had been ordered to return (R. 42-49).

The Commissioner filed a petition for review in the Circuit Court of Appeals, contending in effect that the Board erred in holding that the distributions made by the trustee to the taxpayers were not taxable income in their entirety to the taxpayers (R. 55-59).

That court sustained the contention of the Commissioner, holding that by Section 219 Congress "intended to tax each year to the beneficiary of any trust the share of the trust income which *was distributed* to him in that year," in spite of the fact that what the statute provided the beneficiary should include in his return was "that part of the income of the estate or trust for its taxable year which, pursuant to the instrument or order governing the distribution, is *distributable* to such beneficiary, *whether distributed or not.*" The court also held that the order of the state court was not conclusive upon it in con-

sidering a revenue act, and held that the loss due to depreciation "is borne by remaindermen in determining the tax."

SPECIFICATION OF ERRORS.

The Circuit Court of Appeals erred:

(1) In holding that the taxpayer is taxable upon the amounts received by him and his decedent from the trustee which were not properly distributable to them.

(2) In holding that the order of the state court was not conclusive on the question as to what amounts were properly distributable to the beneficiaries of the trust.

(3) In holding that the trustee was not obliged to withhold from distribution a reasonable allowance for depreciation of the improvements and hotel furniture.

(4) In reversing the decision of the Board of Tax Appeals.

REASONS FOR GRANTING THE WRITS.

(1) The construction of Section 219 of the Revenue Act adopted by the Circuit Court of Appeals is, we submit, not justified by the language of the statute. As Judge Groner said of this statute in his dissenting opinion in *Burnet v. Whitcomb* (decided by the Court of Appeals of the District of Columbia, May 22, 1933):*

> "Fairly construed, I think it cannot be doubted that the true test of liability depends upon whether the income is distributable. If it is, it is taxable whether received or not. If it is not, it would seem

*In this case the majority of the court sustained the contentions of the Commissioner in the case of another beneficiary under the trust here involved.

to me to follow that it is nontaxable, even though received, as, for instance, by mistake."

The majority of the Court of Appeals of the District of Columbia does not definitely decide this point in favor of the present contention of the Commissioner. That opinion relies upon a number of other cases also cited by the Circuit Court of Appeals in another connection which justify an inference contrary to the ruling of the Circuit Court of Appeals on this point. Some of these cases are:

Whitcomb v. Blair, 25 F. (2d) 528, 58 App. D. C. 104;

Hubbell v. Burnet, 46 F. (2d) 446 (C. C. A. 8th), certiorari denied 283 U. S. 840;

Baltzell v. Mitchell, 3 F. (2d) 428 (C. C. A. 1st), certiorari denied 268 U. S. 690.

See also:

Roxburghe v. Burnet, 58 F. (2d) 693 (App. D. C.).

Those cases, either finding or assuming that certain income was distributable, held that it was taxable. They certainly sustain Judge Groner's conclusion from them that, "If it is, it is taxable whether received or not." They seem to compel his final conclusion that, in the converse case, "If it is not * * * it is nontaxable, even though received, as, for instance, by mistake."

Moreover, the construction adopted by the court below is contrary to that which has been placed upon this section for many years by the Treasury Department. As far as we can ascertain, never, until the instant cases (and their companion cases) were argued, did the Commissioner contend that Section 219 of the 1921 Act or similar pro-

visions of previous or later acts should be construed as imposing upon beneficiaries of a trust a tax on money improperly distributed to them.

Each of the Revenue Acts of 1926, 1928 and 1932* contains provisions substantially the same as those of Section 219 of the Act of 1924, and the question here involved is consequently one which arises under the current act as well as under the Act of 1918 and all acts subsequent thereto. Since the Commissioner has changed his previous attitude and the court below has accepted his new view, the question is one which will undoubtedly arise frequently in the future. To our knowledge there are now pending cases involving this very question which will go to the Circuit Court of Appeals for the Eighth Circuit and to the Court of Appeals of the District of Columbia.

The question is consequently an important one in the administration of the Revenue Acts, and we submit that it should be decided authoritatively by this court at this time.

(2) The decision of the Circuit Court of Appeals in the instant case that the order of the state court is not controlling is directly in conflict with the holding of this court in *Uterhart v. United States,* 240 U. S. 598, 603, and the holding of the Circuit Court of Appeals for the Second Circuit in *Commissioner v. Field,* 42 F. (2d) 820, 822. It also disregards the provisions of R. S. Section 905, which provides that the records and proceedings of state courts if properly authenticated "shall have such faith and credit given to them in every court within the United States as they have by law or usage in the courts of the state from which they are taken."

*Section 219 of the Act of 1926, Sections 161-162 of the Act of 1928, and Sections 161 and 162 of the Act of 1932.

(3) The court below, in holding that the trustee should not have maintained a reserve for depreciation, has decided an important question of local law in a way in conflict with the applicable local decisions—*In re Gartenlaub,* 185 Cal. 648, and the decision of the state court in the case of this very trust. Or if the question decided should be considered one of general law, it has been decided in a way probably untenable and in conflict with the weight of authority. (For some of the authorities, see pp. 19-20 *infra.*)

Wherefore it is respectfully submitted that the petition should be granted.

Dated, San Francisco, California,
June 2, 1933.

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BRIEF IN SUPPORT OF PETITION FOR CERTIORARI.

For statement of the case and also statements as to the opinions below, jurisdiction, questions presented, statutes involved and specification of errors, we refer to the foregoing petition.

ARGUMENT.

Although the opinion of the court is in places far from clear, its conclusion must be rested upon one of two propositions which it appears to lay down, both of which we submit are unsound: (1) that the statute must be construed to tax all amounts paid by a trustee to a beneficiary of a testamentary trust as income, even amounts improperly distributed, or (2) that the decree of the state court having jurisdiction over the accounts of the trustee is not controlling here. If it is sought to justify the result on the second of these grounds, the court's conclusion can be sustained only by the establishment of another proposition, which we believe is also unsound—that under the California law the trustee was not required to set up a reserve for depreciation. We will discuss each of these questions briefly.

I.

TAXPAYERS WHO ARE BENEFICIARIES UNDER A TESTAMENTARY TRUST ARE TAXABLE ONLY FOR SO MUCH OF THE AMOUNT RECEIVED BY THEM FROM THE TRUSTEE AS WAS PROPERLY DISTRIBUTABLE TO THEM.

Section 219 of the Revenue Act of 1921 imposes a tax, *inter alia*, upon "income received by estates of deceased persons during the period of administration or settlement of the estate" and "income which is to be distributed to the beneficiaries periodically." Executors, in determining the net income of estates during the period of administration, are allowed to deduct "the amount of any income properly paid or credited to any legatee, heir or other beneficiary." Subdivision (d) of

this section also contains the following provision, which is applicable to both classes of income above mentioned:

> "The tax shall not be paid by the fiduciary, but there shall be included in computing the net income of each beneficiary that part of the income of the estate or trust for its taxable year which, pursuant to the instrument or order governing the distribution, is distributable to such beneficiary, whether distributed or not."

The language above quoted, as well as other parts of this section, indicates clearly that the test of taxability to beneficiaries of income of both of the sorts mentioned is *not actual receipt of money by them, but their legal right to receive the money.* They are taxable only as to income to which they are lawfully entitled.

Section 219 of the previous act—that of 1918—contained similar language. The regulations, which were in force under the 1918 Act at the time when the 1921 Act was passed, provided that each such beneficiary (whether the beneficiary of a trust in which there was income distributable periodically or a legatee of an estate before final settlement to whom income was properly paid) should include in his return "*his distributive share* of the net income, even though not yet paid him, but if the taxable year on the basis of which he makes his returns fails to coincide with the annual accounting period of the estate or trust, then he need only include in his return his distributive share for such accounting period ending within his taxable year."[1] The language of the regulations thus indicated clearly (as indeed the language of the 1918 Act required) that the test of tax-

1. Regulations 45, Article 345, promulgated April 17, 1919.

ability of income was the same for legatees receiving income in the course of the settlement of an estate and for beneficiaries of a trust, the income of which was to be distributed regularly. With this construction in force, Congress passed Section 219 of the 1921 Act, which shows that it approved this construction of the Department. Regulations issued under the 1921 Act[2] were, as to this matter, practically identical with the regulations under the 1918 Act. In Section 219 of the Act of 1924 and in all later acts, Congress reenacted substantially the same language.

Moreover, in Law Opinion No. 1013, promulgated in 1920 (2 C. B. 181, 183), the Solicitor of Internal Revenue, discussing Section 219 of the Act of 1918 relating to the income from trusts, said:

> "It would be highly inequitable and unjust to tax the present beneficiary upon income which is not distributable to him and to which he is not beneficially entitled."

It is, of course, well settled that great weight will be attached to the long adopted construction of tax statutes by the Department of the Treasury. This court has said that a construction "ought not to be disturbed now unless it be plainly wrong."[3]

And where, as here, Congress in subsequent acts has reenacted substantially the same language, that operates as legislative approval of the construction adopted by the Treasury Department.[4]

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2. See Regulations 62, Article 345, 347, pp. vii-viii, *infra*.
3. *Universal Battery Co. v. United States*, 281 U. S. 580, 583.
4. *Brewster v. Gage*, 280 U. S. 327, 336; *McCaughn v. Hershey Chocolate Co.*, 283 U. S. 488, 492-493.

In cases arising under Sections 219 of the various acts, the Commissioner previously took the view that in order to impose a tax on income received by a beneficiary it was necessary to show that he was lawfully entitled to the money. See, for example, *Whitcomb v. Blair,* 58 App. D. C. 104.

As far as we are able to ascertain, it was not until the instant cases were argued that the Commissioner advanced the contention that the statute should be construed to tax a beneficiary of a trust on money paid to him through a mistake of law.

This construction now suggested by the Commissioner would produce most unfair results. The Act of 1921 (like the other Revenue Acts) contains no provision entitling a beneficiary to a deduction if in a later year he repays an amount improperly distributed to him. And in the only case which appears to have arisen involving this exact point, the Commissioner argued and the Board of Tax Appeals held (correctly we submit) that the beneficiary was not entitled to any deduction in the later year in which the amount was repaid.

Pyle v. Commissioner, 16 B. T. A. 218.

The rule, moreover, enforces double taxation in cases like the instant case, thus violating the fundamental principle of our tax system. In the instant case the trustee distributed more than was distributable. According to the rule, as announced, the trustee in such cases is taxable upon the net income, less the amount *distributable,* while the beneficiary is taxed upon the amount *distributed.* The excess of the distribution over the amount distributable is taxed twice, once in the hands of the trustee, who is only allowed to deduct what is *distribu-*

table, and again in the hands of the beneficiary, who is taxed upon everything *distributed.* This is contrary to what has been the uniform ruling under our income tax laws that when income was taxable to the trustee, the beneficiary later receiving the income paid no tax (T. D. 1906; Regulations 33, Article 75, T. D. 1944; Regulations 33, Article 29, revised January 2, 1918).

Such a rule is contrary to numerous decisions of the Board of Tax Appeals, in some of which the Commissioner has acquiesced.[5]

None of the cases cited by the Commissioner in the companion cases to the Court of Appeals for the District of Columbia, in support of his contention that the mere receipt of income by a beneficiary is sufficient to render it taxable, such as *North American Oil Consolidated v. Burnet,* 286 U. S. 417, involved Section 219 of the statute or any section having similar language, or throw any light upon the construction to be given to Section 219. In the *North American Consolidated* case, the Court pointed out that under the provisions of the sections there involved the taxpayer would be allowed a deduction for amounts repaid in a later year, a situation which, as we have pointed out, does not exist in the case of the taxpayer here.

Moreover, we submit that Section 219 of the 1921 Act makes the test of taxability whether the amounts were distributable under the order of the court, where, as here, there was an order of court governing the matter.

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5. *Pyle v. Commissioner,* 16 B. T. A. 218; *White v. Commissioner,* 25 B. T. A. 243; *McCrory v. Commissioner,* 25 B. T. A. 994; *Dixon v. Commissioner,* 25 B. T. A. 1164; *Newbury v. Commissioner,* 26 B. T. A. 101, acquiescence by Commissioner XI I. R. B. No. 32, p. 1; *Boston Safe Deposit and Trust Company v. Commissioner,* 26 B. T. A. 486; *Yukon Alaska Trust v. Commissioner,* 26 B. T. A. 635, acquiescence by Commissioner XI I. R. B. No. 39, p. 1.

II.

THE DECISION OF THE STATE COURT WAS CONTROLLING.

The rights of the parties under the will of A. C. Whitcomb are regulated by the state law,[6] and as this court said in *Uterhart v. United States,* 240 U. S. 598, 603:

> "it is obvious that a judicial construction of the will by a state court of competent jurisdiction determines not only legally but practically the extent and character of the interests taken by the legatees."[7]

Although it is true that the federal courts are not bound in all cases to follow the construction of a will adopted by a state court, they cannot disregard a decision of a state court under which property rights have been settled, where, as here, the question is simply what the property rights are.[8]

This, indeed, is required by R. S. 905.[9]

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6. "The state law creates legal interests but the federal statute determines when and how they shall be taxed." *Burnet v. Harmel,* 287 U. S. 103, 110.

7. *Roberts v. Lewis,* 153 U. S. 367; *Keith v. Johnson,* 271 U. S. 1, 8; *Messenger v. Anderson,* 225 U. S. 436. See, also, *United States v. Kombst,* 286 U. S. 424, 426; *Michigan v. Michigan Trust Co.,* 286 U. S. 334, 342.

8. *Commissioner v. Field,* 42 F. (2d) 820, 822 (C. C. A 2d); *McCaughn v. Girard Trust Company,* 19 F. (2d) 218 (C. C. A. 3rd); *Boal v. Metropolitan Museum of Art,* 19 F. (2d) 454 (C. C. A. 2d), certiorari denied 275 U. S. 565; *Atwood v. Rhode Island Hospital Trust Company,* 34 F. (2d) 18 (C. C. A. 1st), certiorari denied 280 U. S. 600; *Hidden v. Durey,* 34 F. (2d) 174, 178; *Appeal of Appell,* 10 B. T. A. 1225, 1231. See, also, *Wells v. Commissioner,* 63 F. (2d) 425, 438.

9. This section is copied on page i, *infra.*
As said in *Hieston v. National City Bank,* 280 Fed. 525, 526 (App. D. C.):
> "The obligation to accord full faith and credit to a valid judgment, other than for lack of jurisdiction of the person or subject-matter, or for the enforcement of a penalty, is without limitation."
See, to the same effect:
Bradford Elec. Co. v. Clapper, 286 U. S. 145, 155; *Hartford Life Insurance Co. v. Barber,* 245 U. S. 146; *Tilt v. Kelsey,* 207 U. S. 43; *Mitchell v. First National Bank,* 180 U. S. 471.

The argument of respondent that the decision of the state court should be disregarded, because it was not made until after the end of the taxable year here involved, is untenable.[10]

At the time when the Revenue Act of 1921 was passed (it was approved on November 23, 1921), the Commissioner took the position that the decision of local courts as to the distribution of income should control. Law Opinion of the Solicitor of Internal Revenue, No. 1013, promulgated in 1920 (2 C. B. 181, 183), discussing Section 219 of the Act of 1918, relating to the income from trusts, stated that the federal statutes and not the rule of the probate court must govern the question as to what constitutes income, but went on to say:

> "The decisions of the local courts, however, as to the distribution of such items of income are important. *They determine by whom the income should be accounted for.*"

We submit that the statement from the Solicitor's opinion, quoted above, is correct. In any event, it expressed the attitude of the Department when the Revenue Act of 1921 was passed, and the Act of 1921 contains no language indicating that Congress intended to adopt the contrary rule, which the Commissioner seeks to apply in the instant case. Consequently, Congress must be deemed to have approved this construction.[11]

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10. Such was, indeed, the case in the following cases:
United States v. Kombst, 286 U. S. 424, 426; *Michigan v. Michigan Trust Co.*, 286 U. S. 334, 342; *Keith v. Johnson*, 271 U. S. 1, 8; *Messenger v. Anderson*, 225 U. S. 436; *Roberts v. Lewis*, 153 U. S. 367; *Atwood v. Rhode Island Hospital Trust Company*, 34 F. (2d) 18 (C. C. A. 1st), certiorari denied 280 U. S. 600; *Hidden v. Durey*, 34 F. (2d) 174, 178; *Boal v. Metropolitan Museum of Art*, 19 F. (2d) 454 (C. C. A. 2d), certiorari denied 275 U. S. 565; *McCaughn v. Girard Trust Company*, 19 F. (2d) 218 (C. C. A. 3rd); *Appeal of Appell*, 10 B. T. A. 1225, 1231.

11. *Brewster v. Gage*, 280 U. S. 327, 336; *McCaughn v. Hershey Chocolate Co.*, 283 U. S. 488, 492-493.

III.

THE TRUSTEE WAS PROPERLY REQUIRED TO SET UP A RESERVE FOR DEPRECIATION.

Under our view of the case, inasmuch as the state court held that the trustee must set up a reserve for depreciation, it is entirely immaterial whether any other court regards this holding as correct or not. But for the Commissioner to succeed in his view of the case—that the decision of the local court is not binding—it is also necessary for him to establish the further proposition that the decision of the state court was incorrect.

The question, we believe, is a local one. The only applicable local decisions are that of the probate court in the instant case and that of the Supreme Court of the state in *In re Gartenlaub*, 185 Cal. 648. Both support the contention that the depreciation should have been deducted.

Respondent, however, contends that the question is one of general law. Even so, his position is untenable and in conflict with the weight of authorities. Authorities directly supporting the position taken by the probate court in this case are: *Matter of Housman*, 4 Dem. (N. Y.) 404; *Matter of Jones*, 103 N. Y. 621; *In re Crabtree*, 106 Law Times (N. S.) 49; *Hill on Trustees* (Am. ed.), pp. 592, 593. The *Gartenlaub* decision of the California court is in accord with the weight of authority elsewhere.[12]

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12. *Furniss v. Cruikshank*, 230 N. Y. 495; *In re Stevens*, 187 N. Y. 471, 80 N. E. 358, 359-360; *New York Life Insurance & Trust Co. v. Baker*, 165 N. Y. 484, 59 N. E. 257; *In re Murphy's Estate*, 246 N. Y. S. 714; *In re Hall's Estate*, 224 N. Y. S. 376, 381; *In re Golding's Estate*, 216 N. Y. S. 593; *Gould v. Gould*, 213 N. Y. S. 286; *In re Elsner's Will*, 206 N. Y. S. 765; *Kemp v. Macready*, 150 N. Y. S. 618; *Dexter v. Watson*, 106 N. Y. S. 80; *Cairns v. Chaubert*, 9 *Paige's Chancery* 160; *Curtis v. Osborn*, 79 Conn. 555; *New England Trust Company v. Eaton*, 140 Mass. 532; *Healey v. Toppan*, 45 N. H. 243, 266-267; *Ballantine v. Young*,

The particular phraseology of the will in the case at bar emphasizes the pertinency of the foregoing authorities. The testator was dealing with an estate which consisted largely of nondepreciable assets. Naturally he made no specific provision for depreciation. Nevertheless, his gift to the life beneficiaries is only "the interest or income," the remaindermen taking "the whole three thirds parts." This, we submit, must be construed as requiring a reserve to take care of the depreciation on depreciable assets in which the trustee subsequently invested the trust funds.

Dated, San Francisco, California,
June 2, 1933.

Respectfully submitted,
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(Appendix Follows.)

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74 N. J. Eq. 572; *In re Wells' Estate*, 156 Wis. 294, 144 N. W. 174; *In re Allis' Estate*, 123 Wis. 223; *Newbury v. Commissioner*, 26 B. T. A. 101, 106-107; *Hill on Trustees* (Am. Ed.), 592-593; *Perry on Trusts and Trustees*, 7th Ed., Vol. II, pars. 548, 548a.

In the court below the respondent conceded that this court, in *New York Life Insurance Company v. Edward*, 271 U. S. 109, had adopted the rule of the *Gartenlaub* decision.

Appendix

FEDERAL STATUTES.

Revised Statutes, Section 905 (U. S. C. Title 28, Sec. 687):

The acts of the legislature of any State or Territory, or of any country subject to the jurisdiction of the United States, shall be authenticated by having the seals of such State, Territory, or country affixed thereto. The records and judicial proceedings of the courts of any State or Territory, or of any such country, shall be proved or admitted in any other court within the United States, by the attestation of the clerk, and the seal of the court annexed, if there be a seal, together with a certificate of the judge, chief justice, or presiding magistrate, that the said attestation is in due form. *And the said records and judicial proceedings, so authenticated, shall have such faith and credit given to them in every court within the United States as they have by law or usage in the courts of the State from which they are taken.*

Revenue Act of 1921 (c. 136, 42 Stat. 227, 247):

ESTATES AND TRUSTS.

Sec. 219. (a) That the tax imposed by Sections 210 and 211 shall apply to the income of estates or of any kind of property held in trust, including—

(1) Income received by estates of deceased persons during the period of administration or settlement of the estate;

(2) Income accumulated in trust for the benefit of unborn or unascertained persons or persons with contingent interest;

(3) Income held for future distribution under the terms of the will or trust; and

(4) *Income which is to be distributed to the beneficiaries periodically,* whether or not at regular intervals, and the income collected by a guardian of an infant to be held or distributed as the court may direct.

(b) The fiduciary shall be responsible for making the return of income for the estate or trust for ~~which~~ he acts. The net income of the estate or trust shall be computed in the same manner and on the same basis as provided in Section 212, except that (in lieu of the deduction authorized by paragraph (11) of subdivision (a) of Section 214) there shall also be allowed as a deduction, without limitation, any part of the gross income which, pursuant to the terms of the will or deed creating the trust, is during the taxable year paid or permanently set aside for the purposes and in the manner specified in paragraph (11) of subdivision (a) of Section 214. In cases in which there is any income of the class described in paragraph (4) of subdivision (a) of this section *the fiduciary shall include in the return a statement of the income of the estate or trust which, pursuant to the instrument or order governing the distribution, is distributable to each beneficiary,* whether or not distributed before the close of the taxable year for which the return is made.

(c) In cases under paragraphs (1), (2), or (3) of subdivision (a) or in any other case within subdivision (a) of this section, except paragraph (4) thereof the tax shall be imposed upon the net income of the estate or trust and shall be paid by the fiduciary, except that in determining the net income of the estate of any de-

ceased person during the period of administration or settlement *there may be deducted the amount of any income properly paid or credited to any legatee, heir, or other beneficiary.* In such cases the estate or trust shall, for the purpose of the normal tax, be allowed the same credits as are allowed to single persons under Section 216.

(d) In cases under paragraph (4) of subdivision (a), and in the case of any income of an estate during the period of administration or settlement permitted by subdivision (c) to be deducted from the net income upon which tax is to be paid by the fiduciary, the tax shall not be paid by the fiduciary, but *there shall be included in computing the net income of each beneficiary that part of the income of the estate or trust for its taxable year which, pursuant to the instrument or order governing the distribution, is distributable to such beneficiary, whether distributed or not,* or, if his taxable year is different from that of the estate or trust, then there shall be included in computing his net income his distributive share of the income of the estate or trust for its taxable year ending within the taxable year of the beneficiary. In such cases the beneficiary shall, for the purpose of the normal tax, be allowed as credits, in addition to the credits allowed to him under Section 216, his proportionate share of such amounts specified in subdivisions (a) and (b) of Section 216 as are received by the estate or trust.

(e) In the case of an estate or trust the income of which consists both of income of the class described in paragraph (4) of subdivision (a) of this section and other income, the net income of the estate or trust shall

be computed and a return thereof made by the fiduciary in accordance with subdivision (b) and the tax shall be imposed, and shall be paid by the fiduciary in accordance with subdivision (c), except that *there shall be allowed as an additional deduction in computing the net income of the estate or trust that part of its income of the class described in paragraph (4) of subdivision (a) which, pursuant to the instrument or order governing the distribution, is distributable during its taxable year to the beneficiaries. In cases under this subdivision there shall be included, as provided in subdivision (d) of this section, in computing the net income of each beneficiary, that part of the income of the estate or trust which, pursuant to the instrument or order governing the distribution, is distributable during the taxable year to such beneficiary.*

[Subdivision (f) of this section has no possible bearing upon the issues in this case.]

Revenue Act of 1924 (c. 234; 43 Stat. 253, 275):

ESTATES AND TRUSTS.

SEC. 219. (a) The tax imposed by Parts I and II of this title shall apply to the income of estates or of any kind of property held in trust, including—

(1) Income accumulated in trust for the benefit of unborn or unascertained persons or persons with contingent interests, and income accumulated or held for future distribution under the terms of the will or trust;

(2) Income which is to be distributed currently by the fiduciary to the beneficiaries, and income collected by a guardian of an infant which is to be held or distributed as the court may direct;

(3) Income received by estates of deceased persons during the period of administration or settlement of the estate; and

(4) Income which, in the discretion of the fiduciary, may be either distributed to the beneficiaries or accumulated.

(b) Except as otherwise provided in subdivisions (g) and (h), the tax shall be computed upon the net income of the estate or trust, and shall be paid by the fiduciary. The net income of the estate or trust shall be computed in the same manner and on the same basis as provided in Section 212, except that

(1) There shall be allowed as a deduction (in lieu of the deduction authorized by paragraph (10) of subdivision (a) of Section 214) any part of the gross income, without limitation, which pursuant to the terms of the will or deed creating the trust, is during the taxable year paid or permanently set aside for the purposes and in the manner specified in paragraph (10) of subdivision (a) of Section 214, or is to be used exclusively for religious, charitable, scientific, literary, or educational purposes, or for the prevention of cruelty to children or animals or for the establishment, acquisition, maintenance or operation of a public cemetery not operated for profit;

(2) There shall be allowed as an additional deduction in computing the net income of the estate or trust the amount of the income of the estate or trust for its taxable year which is to be distributed currently by the fiduciary to the beneficiaries, and the amount of the income collected by a guardian of an infant which is to be held or distributed as the court may direct, but the amount so

allowed as a deduction shall be included in computing the net income of the beneficiaries whether distributed to them or not. Any amount allowed as a deduction under this paragraph shall not be allowed as a deduction under paragraph (3) in the same or any succeeding taxable year;

(3) In the case of income received by estates of deceased persons during the period of administration or settlement of the estate, and in the case of income which, in the discretion of the fiduciary, may be either distributed to the beneficiary or accumulated, there shall be allowed as an additional deduction in computing the net income of the estate or trust the amount of the income of the estate or trust for its taxable year which is properly paid or credited during such year to any legatee, heir, or beneficiary, but the amount so allowed as a deduction shall be included in computing the net income of the legatee, heir, or beneficiary.

(c) For the purpose of the normal tax the estate or trust shall be allowed the same credit as is allowed to a single person under subdivision (c) of Section 216, and, if no part of the income of the estate or trust is included in computing the net income of any legatee, heir, or beneficiary, then in addition the same credits as are allowed by subdivisions (a) and (b) of Section 216.

(d) If any part of the income of an estate or trust is included in computing the net income of any legatee, heir, or beneficiary, such legatee, heir, or beneficiary shall, for the purpose of the normal tax, be allowed as credits, in addition to the credits allowed to him under Section 216, his proportionate share of such amounts specified in subdivisions (a) and (b) of Section 216 as are, under

this section, required to be included in computing his net income. Any remaining portion of such amounts specified in subdivisions (a) and (b) of Section 216 shall, for the purpose of the normal tax, be allowed as credits to the estate or trust.

(e) If the taxable year of a beneficiary is different from that of the estate or trust, the amount which he is required, under paragraph (2) of subdivision (b) of this section, to include in computing his net income, shall be based upon the income of the estate or trust for its taxable year ending within his taxable year.

[Subdivisions (f), (g) and (h) have no possible bearing upon the issues in this case.]

REGULATIONS OF THE TREASURY DEPARTMENT.

Regulations 62 (1922 Edition) promulgated under Revenue Act of 1921 as approved by the Secretary of the Treasury February 15, 1922:

Art. 345. ESTATES AND TRUSTS TAXED TO BENEFICIARIES. —In the case of (a) a trust the income of which is distributable periodically, (b) an ordinary guardianship of a minor, and (c) an estate of a decedent before final settlement as to any income properly paid or credited as such to a beneficiary, the income is taxable directly to the beneficiary or beneficiaries. Each such beneficiary must include in his return *his distributive share* of the net income, even though not yet paid him, but if his taxable year is different from that of the estate or trust, then he need only include in computing his net income his distributive share of the income of the estate or trust for

its taxable year ending within his taxable year. The regulations governing partnerships are generally applicable to such an estate or trust. See articles 331-335.

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Art. 347. ESTATES AND TRUSTS WITH INCOME WHICH IS DISTRIBUTED PERIODICALLY, AND OTHER INCOME.—In the case of an estate or trust, the income of which consists both of income to be distributed to beneficiaries periodically and other income, the net income of the estate or trust shall be computed and a return thereof made by the fiduciary in accordance with Section 219 (b) and the tax shall be imposed and paid by the fiduciary in accordance with Section 219 (c), except that there shall be allowed as an additional deduction in computing the net income of the estate or trust that part of its income of the class described in Section 219 (a) (4) which, pursuant to the will or trust deed, is distributable during its taxable year to the beneficiaries. *Each of such beneficiaries shall include, in computing his net income, that part of the income of the estate or trust which, pursuant to the instrument or order governing the distribution, is distributable to him during the taxable year.*

Due service and receipt of a copy of the within is hereby admitted

this_____day of June, 1933.

_____

Attorney General of the United States,

_____

Assistant Attorney General of the United States,

_____

General Counsel of the Bureau of Internal Revenue,

Attorneys for Respondent.

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